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In the Supreme Court of the United States

OCTOBER TERM, 1952

No. 142

ESTATE OF HENRY HAUPTFUHRER, DECEASED, HENRY HAUPTFUHRER, JR., GEORGE J. HAUPTFUHRER, AND ALBERT F. HAUPTFUHRER, EXECUTORS, *Petitioners*

v.

COMMISSIONER OF INTERNAL REVENUE

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Third Circuit

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BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The memorandum opinion and findings of fact of the Tax Court (R. 47-62) are unreported. The opinion of the Court of Appeals (R. 76-83) is reported at 195 F. 2d 548.

JURISDICTION

The judgment of the Court of Appeals was entered on April 11, 1952. (R. 84.) A petition for

rehearing was denied on May 8, 1952. (R. 93.) The petition for a writ of certiorari was filed June 20, 1952. The jurisdiction of this Court is invoked under 28 U.S.C., Sec. 1254.

QUESTION PRESENTED

Whether the value of the remainder interests in three separate trusts, which had been created by the decedent in 1933, was includible in his gross estate under Section 811 (d) (2) of the Internal Revenue Code, because of the fact that the decedent had reserved a power to distribute part or all of the principal to the life beneficiaries.

STATUTE AND REGULATIONS INVOLVED

The pertinent provisions of the statute and Regulations involved are set forth in the Appendix, *infra,* pp. 13-19.

STATEMENT

This is a proceeding involving an estate tax deficiency determined by the Commissioner of Internal Revenue (R. 8-15) against the Estate of Henry Hauptfuhrer, deceased (hereinafter referred to as the taxpayer). A number of issues were submitted to the Tax Court for decision (R. 47), but only one of them was brought to the court below on review, and that was the issue as to whether the value of the remainder interests in three *inter vivos* trusts created by the decedent was includible in his gross estate. The facts found

by the Tax Court with respect to that issue (R. 47-50) may be stated as follows:

The decedent, a resident of Pennsylvania, in 1933 created separate trusts for his three sons, George J., Henry, and Albert F. Hauptfuhrer.[1] In each of the trusts, the three sons were named as individual trustees and a corporate trustee was named. In each of the trusts, one of the sons was named life beneficiary and was given a power of appointment[2] over the remainder interest, which upon failure of the power was to go to the surviving children per stirpes, or heirs at law. Each trust instrument also contained a provision permitting the life beneficiary, with the consent of the grantor, to terminate the trust and have distributed to him both the income and principal thereof. (R. 47-48.)

The pertinent provisions of the trust for Henry, which were identical for all material purposes with those of the other trusts, were as follows (R. 48-50):

> In Trust, to pay and distribute the net income from the trust estate at least quarter-

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[1] Copies of the three trust indentures are contained in the record as Petitioners' Exhibits 1, 2 and 3, respectively. (R. 18-46.)

[2] The Tax Court described this as a general power (R. 47) although the sons could appoint only to relatives or charities. (R. 19, 29, 39.) The Court of Appeals properly characterized it as a special power. (R. 81.)

yearly unto Henry Hauptfuhrer, Jr., during his life; and

IN TRUST, during the life of Henry Hauptfuhrer, Jr., to pay and distribute unto him such part or parts or the whole of the principal of the trust estate as he shall, by writing lodged with the Trustees request, provided such request be in writing approved by the Settlor during his lifetime, and after the decease of the Settlor by the Trustees, or a majority of them, and to the extent of such distribution of principal the interests of all persons therein shall be thereby terminated and ended; and

IN TRUST, from and after the death of Henry Hauptfuhrer, Jr., then to pay and distribute the net income from the then remaining trust estate, if any, and the then remaining principal thereof unto and among such person or persons related to Henry Hauptfuhrer, Jr., by blood or marriage and/or for such charities or religious purposes as Henry Hauptfuhrer, Jr., by writing lodged with the Trustees or by last will and testament, shall nominate and appoint, in such manner, at such times and for such interests as he shall determine; and any part of the trust estate, both income and principal, which shall not be or become subject to distribution under the power aforesaid shall be paid and distributed

upon the death of Henry Hauptfuhrer, Jr., unto his then surviving children and issue, children and issue to take by presentation, per stirpes * * *; and

IN TRUST, anything hereinbefore to the contrary notwithstanding, if by reason of misfortune, lack of income or other cause, the share of principal and/or income payable to any person hereunder shall not be sufficient, in the opinion of the Trustees, for the proper care, maintenance, education and support of such person, then the Trustees shall be entitled, in their sole and absolute discretion, to apply out of the principal from which such person is receiving or entitled to receive income, or out of the residuary trust estate, such part or parts thereof as the Trustees shall determine, and to the extent of such application the interest of all persons therein shall be thereby diminished; * * *.

It is hereby expressly stipulated and agreed that all payments of income and/or principal payable to any person hereunder shall, to the fullest extent permitted by law, be free and clear of his or her debts, contracts, engagements, alienations and anticipations, and that the same shall not be liable to any levy, attachment, execution or sequestration.

* * * *

> It is hereby expressly stipulated and agreed that during the life of the Settlor the Settlor shall be entitled to direct and control the exercise by the Trustees hereunder of the powers and authority herein conferred upon the Trustees * * *.
>
> * * * *
>
> The Settlor hereby expressly agrees that the trust created hereby is irrevocable, and that the trust estate and all rights, powers and authority hereunder vested in the Trustees, and their successors, and/or the survivor or survivors of them, upon the date hereof without any right being reserved in the Settlor to receive any principal or income from the trust estate, or to alter, amend or modify any rights or interest therein; and the Settlor hereby ackknowledges this trust and the said assignment and transfer to be irrevocable and to be vested as aforesaid.

In determining the estate tax deficiency, the Commissioner, in addition to making several other adjustments not here material, included in the gross estate the value[3] of the remainder interests in each of the trusts, after the life estates in the three sons, "because * * * the decedent had reserved a power to alter, amend or revoke within the meaning of Section 811 (d)(2) of the Internal Revenue Code." (R. 14, 50.)

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[3] There was no question in the case as to the amounts determined to be the value of the remainder interests.

The Tax Court upheld the Commissioner's action. (R. 50-54.) The court below affirmed. (R. 76-83.)

ARGUMENT

1. Section 811 (d)(2) of the Internal Revenue Code (Appendix, *infra*, pp. 13-14), which applies to transfers made on or prior to June 22, 1936, provides for the inclusion in the gross estate of property transferred (donatively) by the decedent in trust or otherwise, where the enjoyment thereof was subject at his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend, or revoke.

In this case, each of the trust instruments provided that the trustees, with the approval of the settlor (the decedent), could distribute to the life beneficiary all or such part of the principal as he might request. Thus the decedent reserved the power (in conjunction with the trustees, whose action he was expressly empowered to direct and control) to distribute to the life beneficiary all or part of the principal. Because of that reserved power in the decedent to distribute corpus to the sons, the court below upheld the inclusion of the value of the remainder interests in the three trusts in the decedent's gross estate under Section 811 (d)(2) of the Code.[4]

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[4] In addition to holding the remainder interests taxable upon this ground, the Tax Court had also thought them taxable because of the power given the trustees to invade princi-

Through that reserved power, the decedent could convert the limited rights of the sons to absolute dominion over the principal of the trusts, bring about the termination of the trusts and thereby cut off the remainder interests. Clearly, the exercise of the power would have affected the scheme for the enjoyment of the property in such a substantial way as to justify the taxing of the value of the remainder interests under Section 811 (d)(2) of the Code. The decision below is correct, is in keeping with the principles enunciated by this Court in *Commissioner* v. *Estate of Holmes,* 326 U. S. 480, and is in accord with decisions of the lower courts in numerous other cases.[5] No occasion is presented for any further review of the question.

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pal for the proper care, maintenance and education of the life beneficiaries, which provision, in conjunction with the settlor's power to direct the action of the trustees, likewise constituted a power in the settlor within the meaning of Section 811 (d)(2) of the Code. (R. 53-54.) The court below regarded it unnecessary to pass upon that additional ground. (R. 83.)

[5] See, for example, *Mellon* v. *Driscoll,* 117 F. 2d 477 (C.A. 3d), certiorari denied, 313 U.S. 579; *Commissioner* v. *Hofheimer's Estate,* 149 F. 2d 733 (C.A. 2d); *Commissioner* v. *Newbold's Estate,* 158 F. 2d 694 (C.A. 2d); *Thorp's Estate* v. *Commissioner,* 164 F. 2d 966 (C.A. 3d), certiorari denied, 333 U.S. 843; and *Loughridge's Estate* v. *Commissioner,* 183 F. 2d 294 (C.A. 10th), certiorari denied, 340 U.S. 830. See also Treasury Regulations 105, Sec. 81.20. (Appendix, *infra,* p. 15.)

2. The case of *Hays' Estate* v. *Commissioner*, 181 F. 2d 169 (C.A. 5th), with which the decision below is alleged to be in conflict (Pet. 15-16), is clearly distinguishable.[6] There, the reserved power of termination merely would have permitted the same beneficiaries to take earlier the same portion of the trust estate they would have otherwise taken on the grantor's death. Here, the reserved power would have made it possible for the sons to receive principal which they otherwise would not have received—all they could have done otherwise was to appoint to relatives or charities, in default of which the principal would have gone to the children and issue of the sons.

3. The court below correctly rejected (R. 81-83) the taxpayer's contention that the reserved power was not needed because each son could have appointed the remainder in his trust to another son, and then each would agree to exchange the remainder thus received for the remainder in his own trust, with the result that each son would then have a life estate, subject to a spendthrift provision, with a remainder in himself—and since the settlor could waive the spendthrift provision, each trust could thus have been terminated.

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[6] Moreover, there is room for serious doubt whether, in the light of this Court's decision in the *Holmes* case, the *Hays'* case was correctly decided. Cf. *Zirjacks* v. *Scofield* (C.A. 5th), decided June 30, 1952.

As the court below recognized (R. 82), the argument is ingenious, but wholly without merit. It is clear from the trust instruments that, while the grantor was willing to let the sons dispose of the principal after their life estates by appointment to relatives or charities, he was not willing to let the sons take any principal *themselves*—except upon his own approval, or, after his death, the approval of a majority of the trustees. As properly indicated by the court below (R. 82), circumvention by the suggested maneuvers of the plain provisions of the trust instruments, prohibiting the sons from taking for themselves, would not have been possible.[7] In the absence of a reserved power of termination, the sons could not have taken principal. The court below was therefore correct in concluding (R. 83) that the "reserved power of termination was thus not surplusage; it was a vital part of the trust indentures".

Hence, there is no conflict, as alleged (Pet. 9-12), with the decision of this Court in *Helvering* v. *Helmholz*, 296 U.S. 93.

4. The taxpayer concedes the correctness of the decision below if the trusts could not, under

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[7] For the same reason, there is likewise no merit in the other suggested maneuver (Pet. 6), whereby each son would appoint the remainder in his own trust back to the settlor, and the two of them then allegedly could have the trust terminated upon application to a local court.

Pennsylvania law, be terminated without resort to the reserved power in question, but asserts that under the law of that State the trusts could be so terminated. (Pet. 12.) The taxpayer's argument (Pet. 12-15), to the effect that the court below has decided a question of Pennsylvania law in conflict with Pennsylvania decisions, rests on nothing more than the same claimed effect of the suggested maneuvers whereby, it is asserted, termination could have been brought about without resort to the reserved power. As already brought out, the suggested maneuvers would have been ineffective to bring about termination of the trusts in the absence of a reserved power. Here, there were gifts over in default of appointment, and those remainder interests could not have been cut off by the grantor and the sons, in the absence of the reserved power in question. Contrary to the taxpayer's assertion, the court below has correctly interpreted and applied the law of Pennsylvania. See *McCreary Trust,* 354 Pa. 347; *Johnson* v. *Provident Tr. Co. of Phila.,* 280 Pa. 255. See also, *Kamerly Estate,* 348 Pa. 225; *Africa Estate,* 359 Pa. 567; Restatement, Trusts, Sec. 338 (comment f), and Sec. 340 (comment d); and Restatement, Property, Secs. 351-354.

Cases such as *Bowers' Trust Estate,* 346 Pa. 85, *Goodell's Estate,* 53 Pa. D. & C. 13, and *Ammon's Trust Estate,* 52 Pa. D. & C. 509, relied upon by the taxpayer (Pet. 12-15), are clearly inapplicable,

since they involve situations not at all similar to the instant case.[8]

CONCLUSION

The decision below is correct. It turns upon the particular facts of the case and presents no question calling for further review by this Court. There is no conflict of decisions. The petition should, therefore, be denied.

Respectfully submitted,

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Acting Assistant Attorney General.

HARRY MARSELLI,
Special Assistant to the Attorney General.

JULY, 1952.

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[8] Such cases stand for the general proposition, as stated in the *Bowers'* case (346 Pa. at p. 87), to the effect that—

> If all the parties who are or may be beneficially interested in a trust are in existence and sui juris, if there is no ultimate purpose of any kind requiring its continuance, and if all the beneficiaries consent, a court of equity will decree its termination; of course, if there are contingent remaindermen not in existence or not ascertained, the trust cannot be terminated since it is then impossible to obtain the consent of all possible interests.

APPENDIX

Internal Revenue Code:

SEC. 811. GROSS ESTATE.

The value of the gross estate of the decedent shall be determined by including the value at the time of his death of all property, real or personal, tangible or intangible, wherever situated, except real property situated outside of the United States—

* * * * * * *

(d) *Revocable Transfers*—

(1) Transfers after June 22, 1936.— * * *

(2) Transfers on or prior to June 22, 1936.—To the extent of any interest therein of which the decedent has at any time made a transfer, by trust or otherwise, where the enjoyment thereof was subject at the date of his death to any change through the exercise of a power, either by the decedent alone or in conjunction with any person, to alter, amend, or revoke, or where the decedent relinquished any such power in contemplation of his death, except in case of a bona fide sale for an adequate and full consideration in money or money's worth. Except in the case of transfers made after June 22, 1936, no interest of the decedent of which he has made a transfer shall be included in the gross

estate under paragraph (1) unless it is includible under this paragraph;

(3) Date of existence of power.—For the purposes of this subsection the power to alter, amend, or revoke shall be considered to exist on the date of the decedent's death even though the exercise of the power is subject to a precedent giving of notice or even though the alteration, amendment, or revocation takes effect only on the expiration of a stated period after the exercise of the power, whether or not on or before the date of the decedent's death notice has been given or the power has been exercised. In such cases proper adjustment shall be made representing the interests which would have been excluded from the power if the decedent had lived, and for such purpose if the notice has not been given or the power has not been exercised on or before the date of his death, such notice shall be considered to have been given, or the power exercised, on the date of his death.

* * * * * * *

(h) *Prior Interests.*—Except as otherwise specifically provided therein, subsections (b), (c), (d), (e), (f), and (g) shall apply to the transfers, trusts, estates, interests, rights, powers, and relinquishment of powers, as

severally enumerated and described therein, whether made, created, arising, existing, exercised, or relinquished before or after February 26, 1926.

* * * * * * *

(26 U.S.C. 1946 ed., Sec. 811.)

Treasury Regulations 105, promulgated under the Internal Revenue Code:

SEC. 81.20. *Transfers with power to change the enjoyment.*—(a) *Transfers included.*—Subsection (d) of section 811 embraces a transfer by trust or otherwise (if not amounting to a bona fide sale for an adequate and full consideration in money or money's worth) when at the time of decedent's death the enjoyment of the transferred property, or some part thereof or interest therein, was subject to any change through a power exercisable either by the decedent alone, or by him in conjunction with some other person or persons, to alter, or amend, or revoke, or terminate. (See section 81.15.)

The addition to subdivision (d) (1) of the Revenue Act of 1926, by section 805 of the Revenue Act of 1936, of the phrase to the effect that it is not material in what capacity the power was subject to exercise by the decedent or by the other person or persons in conjunction with the decedent (which phrase is also embodied in subsection (d) (1) of section 811 of the Internal

Revenue Code), is considered merely declaratory of the meaning of the subdivision prior to the addition of the phrase.

The second phrase added to this subdivision of the Revenue Act of 1926 by amendment in 1936 (also embodied in section 811 (d) (1) of the Internal Revenue Code), namely, "without regard to when or from what source the decedent acquired such power," is not considered declaratory of the meaning of the subdivision prior to the amendment in a case in which no one of the powers enumerated in the subdivision was reserved at the time of the making of the transfer, but one or more thereof were conferred subsequent thereto (whatever the source from which conferred) without any understanding, expressed or implied, had in connection with the making of the transfer that such power or powers should be later conferred.

The third change made in the subdivision by the Revenue Act of 1936 (which is also embodied in subsection (d) (1) of section 811 of the Internal Revenue Code) consists of the addition of the words "or terminate" following the words "to alter, amend, revoke." Such addition is considered but declaratory of the meaning of the subdivision prior to the amendment. A power to terminate capable of being so exercised as to revest in the decedent the ownership of the transferred property or an interest therein, or as otherwise to inure to his benefit or the benefit of his estate, is, to that extent, the equivalent of a power

to "revoke," and when otherwise so exercisable as to effect a change in the enjoyment, is the equivalent of a power to "alter."

(b) *Taxability.*—The property or any interest therein transferred as described in subsection (a) shall be included in the gross estate if it comes within any one of the following paragraphs:

(1) If the transfer was made prior to the enactment of the Revenue Act of 1924 (4:01 p.m., eastern standard time, June 2, 1924), and the power was reserved at the time of the transfer and was exercisable by the decedent alone or in conjunction with a person or persons having no substantial adverse interest or interests in the transferred property, or if exercisable in conjunction with a person having a substantial adverse interest or with several persons some or all of whom held such an adverse interest, then to the extent of any interest or interests held by a person or persons not required to join in the exercise of the power and to the extent of any adverse interest which was not substantial.

(2) If the transfer was made after the enactment of the Revenue Act of 1924 (4:01 p.m., eastern standard time, June 2, 1924) and before the amendment of the subdivision by the Revenue Act of 1936 became effective (June 23, 1936), and the power was reserved at the time of the transfer and was exercisable by the decedent alone or in conjunction with a person or persons either having or

not having a substantial adverse interest or interests in the transferred property, or in conjunction with persons one or more of whom had and one or more of whom had not such an adverse interest.

(3) If the transfer was made after June 22, 1936 (the date of the enactment of the Revenue Act of 1936), and the power was either reserved at the time of the transfer or later created or conferred, without regard to the source from which the power was acquired, and whether exercisable by the decedent alone or in conjunction with a person or persons either having or not having a substantial adverse interest or interests in the transferred property, or in conjunction with persons one or more of whom had and one or more of whom had not such an adverse interest.

As used in this and in the next succeeding section, the expression "reserved at the time of the transfer" refers to a power to which the transfer was subject when made, whether the power arose by implication of law or by the express terms of the instrument of transfer, and which continued to the date of decedent's death (see the paragraph next following as to the conditions under which the power will be considered as existent at decedent's death) to be exercisable by decedent alone or by him in conjunction with some other person or persons, and includes any understanding, expressed or implied, had in connection with the

making of the transfer that the power should later be created or conferred.

The power to alter, amend, revoke, or terminate will be considered to have existed on the date of the decedent's death, though the exercise of the power was subject to a precedent giving of notice, or though the alteration, amendment, revocation, or termination would take effect only on the expiration of a stated period after the exercise of the power, whether or not on or before the date of the decedent's death notice had been given or the power had been exercised, or though the exercise of the power was restricted to a particular time which had not arrived, or the happening of a particular event which had not occurred, at decedent's death. In determining the value of the gross estate in such cases the full value of the property transferred subject to the power should be discounted for the period required to elapse between the date of decedent's death and the date upon which the alteration, amendment, revocation, or termination could take effect. (See section 81.10 (i) (3).)

The provisions of this section do not apply to a transfer if the power may be exercised only with the consent of all parties having an interest, vested or contingent, in the transferred property, and if the power adds nothing to the rights of the parties as conferred by the applicable local law.

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